

8

Developments in the Financial System

Monetary Policy

Monetary policy in the year 2000 was directed at complementing fiscal policy in supporting economic recovery and facilitating continued financial and corporate sector restructuring. As such, the monetary stance continued to remain accommodative in the first eight months of 2000 to support the growth momentum. A continuation of the easier monetary stance was appropriate given the subdued inflationary environment. The low and stable interest rates and pegged exchange rate regime provided an environment of stability and predictability contributing to the strengthening of consumption and investment. Loan approvals and disbursements have resumed strongly. In the current low interest rate environment loan repayments, have, likewise been high as borrowers have taken advantage to repay their higher cost loans and refinance their borrowings. In 2000, loans outstanding indicated an increasing trend after a relatively stagnant performance in 1999, reflecting a revival in investment.

At the same time, monetary policy aimed at ensuring a positive real rate of interest for depositors. Banking institutions raised their deposit rates following the strengthening of their financial position. As the Bank Negara Malaysia (BNM) intervention rate remained unchanged at 5.50%, the base lending rates (BLR) of banking institutions did not change. Given the uncertainty associated with external developments, the easier monetary stance in 2000 also contributed to ensuring that domestic demand would be sufficiently strong to mitigate any slack in external demand. This is important in sustaining the growth momentum.

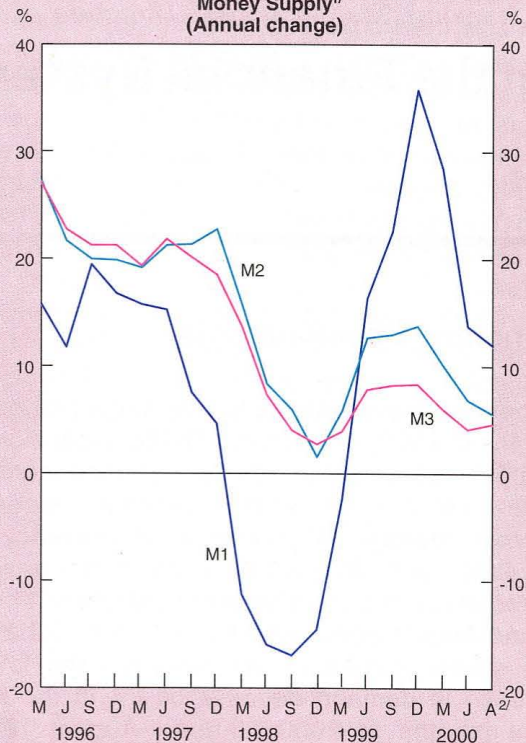
Monetary Developments

Money supply expanded further in the first eight months of 2000, consistent with the expansion in economic activities as well as sustained monthly trade surpluses and level of external reserves. **Narrow money, M1**, comprising currency in circulation and demand deposits of the private sector, expanded at a slower annual rate of 11.9% at end-August 2000 (end-August 1999: 23.2%). The slower growth in M1 reflected the lower increase in demand deposits of 1% in the first eight months of 2000 (January-August 1999: 21.7%) while currency in circulation declined by 18.2% (January-August 1999: 0.6%), reflecting the return of Y2K-related currency in circulation into the system.

Broad money, M2, comprising M1 and narrow quasi-money, constituting private sector holdings of fixed and savings deposits with commercial banks and BNM, net negotiable instruments of deposits (NIDs) and repurchase agreements (repos), recorded a smaller growth of 5.5% at end-August 2000 (end-1999: 13.7%). This was due to the decline in currency in circulation as well as the decrease in quasi-money. The latter expanded at an annual rate of 2.5% during the first eight months of 2000 (January-August 1999: 7.3%). The moderate growth reflected a smaller increase in fixed deposits and to some extent savings deposits placed with commercial banks.

The **broader monetary aggregate, M3**, which comprises M2 and private sector deposits (including repos) placed with other banking institutions, namely, finance companies, merchant banks, discount houses and Islamic banks, but excluding the placement of funds among these institutions, increased more moderately by 4.6% as at end-August 2000 (end-1999: 8.3%).

Chart 8.1
Monetary Trends
Money Supply^{1/}
(Annual change)



In tandem with the continued pick-up in economic activity, the banking system's **total loans and advances** turned around to increase by 3.2% to RM443,906 million in the first eight months of 2000 (January-August 1999: -0.4%). On an annual basis, however, total loan growth was 3.6% (end-August 1999: 0.8%). Commercial banks recorded an increase of 4.1% (end-August 1999: 2.5%) while total loans extended by finance companies increased by 2.4% (end-August 1999: -8.8%). Total loans extended by merchant banks, however, declined by 7.3% (end-August 1999: -5.6%).

Although total loans outstanding registered a moderate increase in the first eight months of 2000, loan approvals, however, registered a significant increase to a monthly average of RM10,848 million (1999: RM8,697 million a month). Similarly, loan disbursements increased to a monthly average of RM28,786 million (1999: RM26,526 million a month). Loan repayments, on the other hand, still remained high, averaging RM28,170 million a month in the period (1999: RM27,744 million a month). In addition, there has been increasing recourse to private debt securities (PDS) for financing. Lending by the banking system was supplemented by a significant increase of 171.4% or RM11,330 million in total PDS outstanding, compared with the same period last year. In aggregate, financing through loans extended by the banking system and PDS increased by RM25,197 million or 5% in the first eight months of 2000. On an annual basis, financing through loans and PDS increased by 12.4% at end-August 2000.

A major portion of the outstanding credit was channelled to finance the broad property sector (36.2%), specifically the purchase of residential property, manufacturing activities (15.5%) and consumption credit (12.8%) as at end-August 2000, as shown in *Table 8.2*. Of the total new loans approved, 32.9% was extended to the broad property sector while 18.2% and 15.7% was extended to the consumption and manufacturing sectors respectively. In terms of loans disbursed, the manufacturing, broad property and consumption sectors accounted for 25.8%, 18.6% and 11.9%, respectively of the total in the period, which amounted to RM230,284 million.

Table 8.2
Banking System Banks: Direction of Lending
(including Islamic banks)

	Change During Period				As at End-August 2000
	1999		2000		
	January-August		January-August		
	RM million	%	RM million	%	RM million
Agriculture	409.9	5.2	650.9	6.9	10,148.2
Mining and quarrying	-162.8	-9.3	24.8	1.5	1,675.4
Manufacturing	763.7	1.2	2,727.3	4.1	68,773.1
General commerce	320.9	0.9	1,469.1	4.0	38,204.7
Broad property ¹	-167,883.4	-51.8	6,188.3	4.0	160,833.4
Transport and storage	424.4	2.8	-1,270.3	-8.1	14,352.2
Finance, insurance and business services	-5,020.2	-13.2	-1,170.8	-3.4	32,892.6
Consumption credit	-680.1	-1.4	5,934.5	11.6	56,875.4
Purchase of securities	-3,027.2	-8.0	-632.6	-1.9	33,200.8
Miscellaneous	173,307.4	118.8	-54.1	-0.2	26,950.1
Total²	-1,547.4	-0.4	13,867.1	3.2	443,905.6

¹ Including loans sold to *Cagamas Berhad*.

² Including loans sold to *Danaharta*.

Source: *Bank Negara Malaysia*.

Liquidity in the banking system remained ample in the first eight months of 2000 mainly due to the sustained monthly trade surpluses. Reflecting the higher increase in loans relative to deposits, the banking system experienced a narrowing of resource surplus of RM5,833 million during the period (January-August 1999: RM26,524 million). This resulted in an increase in the loan-deposit ratio to 84.6% at end-August 2000 (end-1999: 83.2%). Commercial banks and finance companies registered a higher loan-deposit ratio of 85.1% and 87.2%, respectively (end-1999: 83.9% and 83.5%, respectively) while merchant banks experienced a decline in the loan-deposit ratio to 68.4% (end 1999: 72.9%).

The ample liquidity situation continued to exert downward pressure on **interest rates** in the first seven months of 2000. This led the average BLR of commercial banks to decline to an all-time low of 6.75% since May 2000. The BLR of finance companies breached the historical low of 8.40% registered at end-1994 to stand at 7.95%. Deposit rates, similarly, declined further in the first seven months of 2000. The 3-month fixed deposit rates of both commercial banks and finance companies declined to 3.26% and 3.30%, respectively at end July-2000 (end-July 1999: 3.75% and 3.80%, respectively). However, in August, banking institutions raised their deposit rates. Following this increase, the 1-month to 12-month fixed deposit rates of commercial banks ranged between 3.44% - 4.10% at end-September (end-1999: 3.24% - 3.95%). Similarly, the average savings deposit rate of commercial banks increased marginally by four basis points to 2.81% while that of finance companies declined marginally by 13 basis points to 3.34%. As inflation was benign at 1.4% during the first eight months of the year, depositors continued to earn a positive real rate of return.

The banking system continued to remain strong in tandem with the improving economy. The risk-weighted capital ratio (RWCR) of the banking system improved to 13.1% at end-August 2000 (end-1999: 12.5%) while the net non-performing loan (NPL) ratio (6-month classification) was 6.9% at end-July 2000 (end-July 1999: 7.9%), down from a peak of 9% at end-November 1998.

Aside from maintaining an accommodative monetary policy stance, BNM actively assisted in generating new funds to finance development. In the first eight months of the year, the following funds were established:

- *Tabung Projek Usahawan Bumiputera* with an allocation of RM300 million was established on 10 February 2000, to provide financing at a reasonable cost to Bumiputera Small and Medium Enterprises (SMEs);
- A Fund for Small and Medium Industries 2, with an allocation of RM200 million, was established on 15 April 2000 to promote SMLs with linkages to export-oriented industries; and

- An Enterprise Programme was launched on 9 June 2000, to expedite the resolution of NPL problems of SMEs.

Financial and Corporate Sector Restructuring

In the first eight months of 2000, further progress was made in the restructuring of both the banking and corporate sectors. By end-August 2000, *Danaharta* had acquired and managed loans, amounting to RM46,785 million (August 1999: RM39,285 million) from the financial system, comprising a total of 2,744 loan accounts (August 1999: 2,273 loan accounts). NPLs from the banking system managed by *Danaharta* amounted to RM38,610 million or 43.2% of total NPLs in the banking system. In return for NPLs acquired, *Danaharta* has, to date, issued RM11,140 million in face value of Government-guaranteed bonds with a present value of RM8,215 million and paid RM800 million in cash to the selling financial institutions, making a total fair purchase price of RM9,015 million. The last bond issue of RM328 million was made at end-March 2000.

Danaharta has, to date, made significant progress in managing the acquired NPLs and disposing of some of the assets acquired from financial institutions. Up to end-August 2000, *Danaharta* has initiated recovery action on 99% of NPLs under its portfolio. *Danaharta* has also conducted three property tender exercises which netted RM333 million from the sale of 209 properties. As at end-August, a total of RM21,567 million loans or assets had been restructured or disposed with an average recovery rate of 75%.

Since its establishment in August 1998, *Danamodal* has injected RM7,590 million capital into 10 banking institutions in the form of Exchangeable Subordinated Capital Loans. With the improvement in the Malaysian economy, five banking institutions made full repayment while two made partial repayment amounting to RM2,730 million. As at end-August 2000, outstanding recapitalisation in the remaining five banking institutions stood at RM4,860 million. While the RWCR of each recapitalised banking institution remained stable at above 10%, the average RWCR of the recapitalised banking institutions declined to 12.2% at end-August 2000 (end-1999: 13.3%) due to the expansion of risk-weighted assets following the resumption of lending.

The Corporate Debt Restructuring Committee (CDRC) has made considerable progress in corporate restructuring. As at end-August 2000, CDRC has received 75 applications with debt totalling RM45,939 million, of which 38 restructuring schemes involving debt of RM25,693 million have been resolved. Of the 38 cases, 29 involving debt of RM23,879 million have been completed or are in the process of being implemented, with another nine cases worth RM1,814 million transferred to *Danaharta*. CDRC is currently reviewing 20 cases involving debt of RM16,343 million. In addition, CDRC was also involved in the restructuring of the transportation industry involving RM7,904 million, of which RM136 million debt has been restructured while RM4,543 million debt for a telecommunications company is now in the implementation stage.

In line with the need to develop a core of strong and forward-looking domestic banking institutions, a consolidation exercise aimed at reducing the existing large number of domestic financial institutions into 10 banking groups is currently being undertaken. On 14 February 2000, the Government announced the formation of 10 banking groups. As at end-August 2000, all banking institutions successfully concluded merger negotiations and signed the sales and purchase agreements, thus qualifying for the merger incentives accorded by the Government. The merger programme is scheduled to be completed by end-2000.

A comprehensive Master Plan for the Malaysian financial system is being developed with the objective of building the foundation and charting the strategic directions of the banking sector for the coming decade. This includes formulating strategies and action plans to increase the resilience, competitiveness and dynamism of the banking institutions in meeting the increasing challenges of globalisation and liberalisation.

Islamic Banking

Islamic banking continued to expand in tandem with the improved economic conditions. Apart from *Bank Islam Malaysia Berhad* and *Bank Muamalat Malaysia Berhad*, 49 other financial institutions (21 commercial banks, 16 finance companies, five merchant banks and seven discount houses), offered Islamic banking services under the Islamic Banking Scheme as at end-August 2000. Total

assets of the Islamic banking system (Islamic banks and Islamic Banking Scheme) increased by 17% during the first eight months of 2000 to RM41,833 million at end-August 2000 (end-August 1999: RM30,737 million). Total deposits mobilised increased by 25.4% to RM31,015 million during the period while financing extended by the Islamic banking system increased by 24.1% to RM17,377 million. The bulk of new deposits was from investment deposits which registered an increase of 35.9% to RM22,395 million. Savings deposits increased by 21.6% to RM2,913 million while current deposits declined by 20.5% to RM4,355 million during the period.

In terms of direction of lending by sector, a major proportion of the financing was channelled to the residential property sector which constituted 20.6% of total financing while 13.3% was extended to the transportation sector and 10.4% to the manufacturing sector. The value of transactions recorded in the Islamic interbank money market was RM202,249 million during the period January-August 2000 (January-August 1999: RM288,426 million).

Several measures were introduced as part of ongoing efforts to strengthen the development of Islamic banking. They included, among others, the setting up of a second Islamic bank, *Bank Muamalat Malaysia Berhad*, which commenced operations on 1 October 1999 and the appointment of the two Islamic banks as agents for the *Mudharabah* operations on 21 January 2000.

Development Finance Institutions

Development finance institutions (DFIs) are institutions established primarily for the purpose of promoting development in the agriculture and manufacturing sectors, infrastructure as well as exports and international trade. Total resources of DFIs increased by RM4,520 million or 26.4% to RM21,672 million at end-June 2000 (end-June 1999: RM17,152 million). The increase in resources was funded mainly by borrowings and capital funds as DFIs are not licensed to mobilise deposits from the public. Borrowings of DFIs surged by 39.3% to RM7,663 million (end-June 1999: RM5,051 million), mainly due to increased borrowings by *Bank Industri dan Teknologi Malaysia Berhad*, *Bank Pembangunan dan Infrastruktur Malaysia Berhad* and *Bank Pertanian Malaysia*

to account for 76.4% of total borrowings. Capital funds of DFIs increased by 35% to RM2,949 million (end-June 1999: RM2,186 million).

Loans approved by DFIs declined by 85.1% to RM772 million (end-June 1999: RM5,198 million), as shown in *Table 8.3*. The decline was largely on account of the decline in loans for infrastructure projects extended by *Bank Pembangunan dan Infrastruktur Malaysia Berhad* as these loans had increased significantly in the previous year. In terms of distribution by sector, loans extended to the agriculture sector increased by 126.5% to RM299 million (end-June 1999: RM132 million) to account for the largest share (38.7%). Loans to the manufacturing sector declined by 26.2% to RM240 million (end-June 1999: RM325 million). Despite the decline, the manufacturing sector accounted for a significant share of total loans extended by DFIs (31.1%).

Several specialised assistance schemes continue to be implemented by DFIs and other participating financial institutions, as shown in *Table 8.4*. The aim of these funds was primarily to assist Small and Medium Industries (SMIs) and SMEs as well as entrepreneurs. Two funds, namely, the **Bumiputera Industrial Fund** and the **Fund For Small and Medium Industries** were terminated on 3 April 2000, as the funds were almost fully utilised. Applications received prior to this date

will, however, still be considered for approval. Eligible borrowers under the *Bumiputera Industrial Fund* can also continue to get financing under the New Entrepreneurs Fund (NEF).

Two new funds were established, namely, the **Tabung Projek Usahawan Bumiputera (TPUB)** on 10 February 2000 and the **Fund for Small and Medium Industries 2 (FSMI 2)** on 15 April 2000. FSMI2 is administered by the Credit Guarantee Corporation while TPUB is managed by ERF Sdn. Bhd., a subsidiary of BNM. TPUB was established with an allocation of RM300 million to assist small-and-medium-scale *Bumiputera* entrepreneurs and wholly-owned *Bumiputera* companies that have difficulties in obtaining financing from financial institutions to undertake new projects or to continue with viable projects in hand in the construction, supply, manufacturing and services sectors. However, the loan under TPUB is to be utilised solely as working capital. The interest charged is 5% per annum. Up to end-August 2000, 82 applications amounting to RM40 million have been approved, with disbursements of RM15 million for 35 cases. Following the termination of the Fund for Small and Medium Industries, the Government launched FSMI 2 with an allocation of RM200 million. The objective of the fund is to provide financing to SMIs in the manufacturing and services sectors to assist them in penetrating the export market or providing linkages to export-oriented companies. As at end-August 2000, 86 applications valued at RM44 million have been approved with disbursements of RM11 million.

Other major changes in the specialised assistance schemes were as follows:

- The **ASEAN-Japan Development Fund** receives funding allocations from the Overseas Economic Cooperation Fund (OECF) and the Export-Import Bank of Japan (JEXIM). OECF and JEXIM, however, were merged on 1 October 1999, and is now known as the Japan Bank for International Cooperation (JBIC).
- Effective 3 April 2000, the maximum loan allowed per customer under the NEF was increased from RM2 million to RM3 million and the NEF guideline was amended to enable participants of the vendor development programme to apply for financing under this scheme.

Table 8.3

**Direction of Lending by DFIs
(end-June)**

Sector	(RM million)		% share	
	1999	2000 ^P	1999	2000
Manufacturing	325	240	6.3	31.1
Agriculture	132	299	2.5	38.7
Real estate & construction	1,229	33	23.6	4.3
Transport & storage	3,445	140	66.3	18.1
Others	67	60	1.3	7.8
Total	5,198	772	100.0	100.0

^P Preliminary data.

Source: *Bank Pertanian Malaysia, Bank Pembangunan dan Infrastruktur Malaysia Berhad, Malaysian Industrial Development Finance Berhad, Bank Industri & Teknologi Malaysia Berhad, Export-Import Bank of Malaysia, Sabah Development Bank, Perbadanan Pinjaman Sabah and Borneo Development Corporation.*

Table 8.4

Specialised Assistance Schemes in the Financial System (end-August 2000)

Type of Fund	Allocation (RM million)	Amount approved (RM million)	No. of cases Approved	Amount drawdown (RM million)
1. Enterprise Rehabilitation Fund* ¹	500	297.9	—	297.9
2. New Entrepreneurs Fund*	1,250 ²	1,336.6	2,825	1,151.5
3. Special Fund for Tourism* ³	200 ⁵	214.7	199	199.3
4. Industrial Adjustment Fund ⁴	500	95.0	25	95.0
5. Ship Financing Facility*	600 ⁶	549.1	34	520.7
6. Fund for Food	1,000 ⁶	656.6	2,451	598.2
7. Bumiputera Industrial Fund ⁷	100	98.7	100	90.7
8. Fund for Small and Medium Industries ⁷	1,850	4,241.9	5,846	3,226.4
9. Rehabilitation Fund for Small and Medium Industries	500	267.0	257	210.3
10. Special Scheme for Low and Medium Cost Houses*	1,000	796.6	106	423.2
11. Asean-Japan Development Fund*		1,956.5	4,371	1,956.5
12. Fund for Small and Medium Industries 2	200	43.6	86	11.0
13. Tabung Projek Usahawan Bumiputera	300	40.3	82	14.6

* Including RM300 million allocated for *Persatuan Peladang Kawasan*.

* Revolving credit.

¹ Figures as at end-July 2000.

² Expiry date of receiving applications was December 1990. Starting September 1995, contingent liabilities are not included in amount approved.

³ Initial allocation was RM400 million with additional allocations of RM200 million on 11 April 1994 and RM200 million on 21 December 1994.

⁴ Terminated on 31 December 1997. BNM is still monitoring the repayment and disbursement of the funds.

⁵ Terminated on 4 August 1999.

⁶ Initial allocation was RM120 million with an additional allocation of RM80 million on 16 November 1993.

⁷ Initial allocation was RM300 million with an additional allocation of RM300 million on 28 October 1994.

⁸ Terminated on 3 April 2000.

Source: Bank Negara Malaysia, ERF Sdn. Bhd., Bank Pertanian Malaysia, Bank Pembangunan dan Infrastruktur Malaysia Berhad, Malaysian Industrial Development Finance Berhad, and Bank Industri & Teknologi Malaysia Berhad.

As at end-August 2000, 16,382 cases were approved under the various funds to total RM10,595 million (end-1999: 14,247 cases worth RM9,250 million). Disbursements increased by 27.6% to RM8,795 million (end-1999: RM6,891 million), particularly to SMIs and the housing sector was in tandem with the expansion in economic activities during the period.

Other Financial Institutions

Discount Houses

Overall performance of discount houses declined in the first eight months of 2000, as reflected in the 11.7% reduction in total deposits (including repos) mobilised by discount houses to RM8,944 million (January-August 1999: 0.4%). Of the total deposits, 4.1% was placed by commercial banks, with the balance from other financial institutions.

Total investment of discount houses recorded a marginal increase of 7.8% in the first eight months of 2000, to RM17,346 million at end-August 2000 (January-August 1999: 4.1%). Investment in *Cagamas* bonds increased by 146.3% to RM1,114 million in the period (January-August 1999: 295%). Investment in PDS by discount houses, however, posted a 21.3% decline to RM19,111 million (January-August 1999: 863.2%) while investment in Bankers Acceptances (BAs) increased by 14.2% to RM3,638 million (January-August 1999: -19.1%). Investment by discount houses in Malaysian Government Securities (MGS) and NIDs declined during this period by 56.9% and 63.4%, respectively (January-August 1999: 144.5% and -49.9%, respectively).

Following the annual review of the Principal Dealer System by BNM in 2000, two new discount houses were appointed as principal dealers. As at end-August 2000, seven discount houses were in operation.

National Savings Bank

Total resources of the National Savings Bank (BSN) increased by 8.3% to RM9,629 million at end-June 2000 (end-June 1999: RM8,893 million), mainly due to a 15.4% increase in **deposits** mobilised by BSN to RM9,030 million (end-June

1999: RM7,826 million) on account of an increase in the number of account holders to 8.9 million (end-June 1999: 8.3 million), as shown in *Table 8.5*. The increase in deposits was mainly from fixed deposits, GIRO and Islamic Banking Scheme, comprising *Skim Al-Mudharabah* and *Skim Al-Wadiah*.

Table 8.5

National Savings Bank
(as at end-June)

	1999	2000 ^P
Deposits¹ (RM million)	7,826.30	9,029.71
Savings	1,393.13	1,380.22
Fixed	3,189.69	4,048.70
Save-As-You-Earn	13.89	14.58
GIRO	2,560.23	2,805.78
Premium Savings Certificates	538.60	569.57
Islamic Banking Scheme	130.76	210.71
CHESS	-	0.15
Investments at book value (RM million)	5,892.77	6,658.42
MGS	2,142.73	2,173.77
Stocks and shares ²	1,351.50	1,179.49
Others ³	2,398.54	3,305.16
Gross Loans (RM million)	2,177.02	2,041.32
Individuals	1,165.77	1,277.49
Corporate	275.50	49.06
Credit Cards	31.84	34.42
Hire-purchase	660.43	622.21
Staff	43.48	58.14
Number of BSN branches ⁴	446	438
Number of post offices with BSN facilities	645	641
Number of depositors ('000)	8,308.44	8,968.40
Savings	2,580.41	2,586.63
Fixed	233.89	179.70
Save-As-You-Earn	14.36	12.50
GIRO	5,479.78	6,188.96
CHESS	-	0.61

¹ Includes interest credited.

² Includes trustee and non-trustee shares, private debt securities and warrants.

³ Includes long and short-term deposits, investments in subsidiary and associated companies.

⁴ Includes mini and sub-branches.

^P Preliminary data.

Source: National Savings Bank.

In consonance with the increase in total resources, investments rose 13% to RM6,658 million (end-June 1999: RM5,893 million). BSN continued to invest a major proportion of its resources in short and long-term deposits as well as in subsidiaries and associated companies, amounting to RM3,305 million or almost half of total investments. **Lending** activities of BSN declined by 6.2% to RM2,041 million at end-June 2000 (end-June 1999: RM2,177 million) mainly due to a decline in corporate loans and hire-purchase financing. The bulk of loans continued to be extended to individuals totalling RM1,277 million (62.6% of total loans), followed by loans for hire-purchase financing which amounted to RM622 million (30.5% of total loans).

Due to the merging of some branches, the total number of BSN branches was reduced to 438 at end-June 2000 (end-June 1999: 445). BSN facilities continue to be provided in 641 post offices.

Pension and Provident Funds

Total resources mobilised by the nine provident and pension funds (PPFs), comprising the Employees Provident Fund, the Social Security Organisation, the Armed Forces Fund, the Pensions Trust Fund and five other private PPFs, continued to grow. The increase in total resources was 13.4% to RM201,614 million at end-June 2000 (end-June 1999: RM177,713 million), as shown in *Table 8.6*. Net contributions continued to increase, amounting to RM10,263 million (end-June 1999: RM7,989 million) in tandem with the increase in the number of contributors and improving incomes due to the economic recovery.

The **Employees Provident Fund (EPF)** accounted for RM172,507 million or 85.6% of total resources of PPFs at end-June 2000. The increase in resources was due to a 13.8% rise in contributions to RM172,159 million (end-June 1999: RM151,233 million) and a 14.5% increase in income from investments to RM6,185 million (end-June 1999: RM5,404 million). EPF membership (inclusive of foreign workers) continued to increase, reflecting the improved labour market conditions with membership at 9.7 million (end-June 1999: 9.4 million). EPF continued to invest substantially in MGS accounting for RM58,259 million or one-third of total investments. Investments in corporate securities and bonds rose significantly by 18.2% to RM50,417 million (end-June 1999: RM42,643 million).

Table 8.6

Provident and Pension Funds
(RM million)
(end-June)

	Total Resources		Malaysian Government Securities		Net Contribution	
	1999	2000 ^P	1999	2000 ^P	1999	2000 ^P
EPF	151,576	172,507	46,987	58,259	3,911	4,792
SOCSCO	7,034	8,232	2,489	3,242	233	208
AFF	4,683	4,836	5	0	(109)	(181)
KWAP	13,563	15,126	0	0	3,956	5,455
Private PPFs	857	913	222	114	(1.7)	(11)
Total	177,713	201,614	49,703	61,615	7,989	10,263

^P Preliminary data.

Figures in parentheses indicate net withdrawals.

Source: Employees Provident Fund, Social Security Organisation, Armed Forces Fund, Pensions Trust Fund and five other private provident and pension funds (Malaysian Estates Staff Provident Fund, MAS Malaysia Provident Fund, SESCO Employees Provident Fund, Petronas Retirement Benefit Scheme and Jendarata-Bernam Provident Fund).

million), reflecting the more favourable equity market during the first half of the year and the pick-up in the corporate bond market.

The **Social Security Organisation (SOCSCO)** was established under the Employees Social Security Act 1969 to provide security benefits to workers. Total resources mobilised by SOCSCO rose 17% to RM8,232 million at end-June 2000 (end-June 1999: RM7,034 million). The bulk of SOCSCO's resources was invested in MGS (RM3,242 million or 39.4% of total investments), followed by investments in bank deposits (RM3,135 million or 38.1% of total investments). Investments in corporate securities increased significantly by 77.7% to RM1,043 million (end-June 1999: RM587 million).

The **Armed Forces Fund (AFF)** was established to provide superannuation benefits to servicemen in the armed forces. Total resources mobilised by AFF rose slightly by 3.3% to RM4,836 million at end-June 2000 (end-June 1999: RM4,683 million). Net contributions remained negative on account of higher withdrawals of RM308 million (end-June 1999: RM157 million). During the period under review, AFF invested largely in trust funds, accounting for RM3,580 million or 75.9% of total investments.

The **Pensions Trust Fund (KWAP)** was established under the Pensions Trust Fund Act 1991 to assume the Government's obligations in meeting the cost of pension and gratuity payments of the public sector. Total resources mobilised by

KWAP rose 11.5% to RM15,126 million at end-June 2000 (end-June 1999: RM13,563 million) on account of a 32.9% rise in funds contributed by the Federal and state governments as well as local authorities and statutory bodies with a 41.3% increase in refund of employers' contribution to EPF and other approved funds. The investment portfolio of KWAP remained the same as in the previous years with the bulk of investments in deposits and money market instruments (48.8%), equity and trust funds (28.9%) as well as corporate loans and bonds (16.6%). Of significance is the 241.4% increase in corporate loans and bonds to RM1,451 million (end-June 1999: RM425 million), reflecting the pick-up in the corporate bond market.

Total resources of the five private PPFs rose 6.5% to RM913 million at end-June 2000 (end-June 1999: RM857 million). The bulk of the resources continued to be invested in corporate securities and bonds (45.8%), followed by investment in deposits and money market instruments (24.8%). Investment in MGS, however, declined to RM114 million to account for 12.5% of total investment (end-June 1999: RM222 million or 25.9% of total investment). Net contribution of the five PPFs continued to remain negative on account of higher net withdrawals.

Insurance Companies

In line with the overall improvement in the economy, the **insurance industry** comprising life insurance and general insurance continued to grow in the first six months of 2000. Premium income of **life insurance** increased by 23.8% to RM3,902 million (January-June 1999: RM3,151 million), as shown in *Table 8.7*. Investment-linked business increased significantly by nearly 19 times in terms of new business premiums during the period. Total assets of life insurance funds increased by 19.2% to RM34,382 million at end-June 2000, as shown in *Table 8.8*. Corporate securities continued to be the largest component, accounting for RM14,915 million or 43.4% of total assets (end-June 1999: 35.7%).

Gross direct premiums of **general insurance** turned around to record a positive growth of 7.3% to RM2,932 million in the first six months of 2000

Table 8.7

Life and General Insurance Business

	End 1999	End-June 2000 ^P
Life insurance business (RM million)		
New business:		
Number of policies ('000 units)	1,437.1	557.5
Sums insured	99,854.6	60,090.9
Total premiums	1,910.7	1,221.8
Business in force		
Number of policies ('000 units)	6,998.7	7,032.3
Sums insured	363,929.0	386,394.1
Annual premiums	6,842.7	7,073.4
Premium income	7,033.9	3,902.1
Benefit payments		
Total	2,232.1	1,149.5
Maturity	530.1	244.4
Death & disability	700.1	385.6
Surrender	577.2	296.5
Medical	88.0	55.7
Cash bonuses	335.5	167.3
Annuity	n.a.	n.a.
General Insurance (RM million)		
Premium Income:		
Gross direct premiums	5,269.5	2,932.3
Net premiums	4,464.9	2,390.0
Reinsurance placed outside		
Malaysia	650.9	318.0
Retention ratio (%) ¹	84.7	81.5
Number of insurance companies		
Direct:		
Life	7	7
General	38	37
Composite	11	11
Reinsurance:		
Life	1	1
General	10	9
Composite	—	1
Number of takaful operators	2	2

^P Preliminary data.

¹ Net premiums over gross premiums.

n.a. — not available.

Source: *Bank Negara Malaysia*.

(January-June 1999: RM2,732 million). All classes of general business registered positive growth with motor at 13.1% to RM1,298 million, followed by miscellaneous at 4% to RM706 million, marine, aviation and transit at 2.6% to RM233 million and fire at 2.5% to RM696 million (January-June 1999: RM1,147 million, RM679 million, RM227 million

Table 8.8

Life and General Insurance Business
(RM million)

	Life Insurance		General Insurance	
	End-1999	End-June 2000 ^P	End-1999	End-June 2000 ^P
Fixed assets	294.5	327.9	602.5	598.7
Loans	5,886.2	5,816.3	438.3	422.5
Government papers	4,243.1	4,993.0	1,895.5	1,942.1
Government guaranteed loans	120.6	145.3	36.3	115.1
Corporate and debt securities	12,962.4	14,914.8	3,439.8	3,973.6
Investment properties	1,624.4	1,721.8	378.9	378.6
Cash and deposits	5,013.2	5,103.7	5,042.8	5,110.8
Others assets	1,341.1	1,359.1	1,466.0	1,574.9
Total	31,485.4	34,382.0	13,300.1	14,116.3

^P Preliminary data.

Source: *Bank Negara Malaysia*.

and RM679 million, respectively). Motor insurance continued to dominate the general sector in terms of market share, accounting for 44.3% of total gross direct premiums, followed by miscellaneous with 24.1%. Total assets of general insurance funds grew by 4.5% to RM14,116 million at end-June 2000 (end-June 1999: RM13,510 million). Cash and deposits remained the largest component, accounting for RM5,111 million or 36.2% of total general insurance funds, followed by corporate and debt securities with RM3,974 million or 28.1%.

As at end-September 2000, 63 insurers, comprising seven life insurers, 10 composite insurers, 36 general insurers, eight general reinsurers, one life reinsurer and one composite reinsurer, were in operation. Of the total, 53 were Malaysian-incorporated with the remaining being foreign-incorporated. At the same time, there were two *takaful* operators, 36 licenced brokers and 41 licenced loss adjusters.

Takaful Business

The Malaysian **takaful industry** consists of two *takaful* operators, namely, *Syarikat Takaful Malaysia Berhad* (STMB) and *Takaful Nasional Sdn. Berhad* (TNSB). Based on preliminary data for the 2000 financial year, the *takaful* industry sustained its growth momentum with the main business indicators recording higher double-digit growth rates. Combined assets of *takaful* funds and shareholders' funds increased by 34.1% to RM1,319 million at end-2000 financial year (end-1999: RM984 million), largely attributable to the favourable growth in family *takaful* business, as shown in *Table 8.9*. Assets of family *takaful* funds accounted for 66.3% of total assets, general *takaful* funds 21.1%, with the balance of 12.6% being assets of shareholders' funds. Investment in Government Investment Certificates amounted to RM142 million or 10.8% of total assets while investment accounts with *Bank Islam Malaysia Berhad* totalled RM106 million or 8.1% of total assets.

Table 8.9

Family and General *Takaful* Business

	Financial Year 1999	Financial Year 2000 ^P
Assets ¹ (RM million)	984.1	1,319.4
Malaysian Investment Certificates	89.8	142.3
Investment in Bank Islam Malaysia Bhd.	41.3	106.2
Corporate securities	124.0	177.4
Cash and deposits	9.5	5.0
Financing	99.2	101.0
Fixed assets	124.4	122.5
Others ²	495.9	665.0
Family <i>takaful</i> business		
New business:		
Total contribution (RM million)	154.6	261.7
Sums participated (RM million)	5,996.3	15,574.2
Number of certificates	100,551	154,470
Business in force:		
Total contribution (RM million)	239.6	319.8
Sums participated (RM million)	19,031.4	29,262.0
Number of certificates	279,491	436,573
General <i>takaful</i> business		
Gross contributions (RM million)	142.8	177.2
Net claims paid (RM million)	24.2	30.9

^P Preliminary data.¹ Assets of family *takaful* funds, general *takaful* funds and shareholders' funds.² Includes shares, cash and other assets.Source: *Syarikat Takaful Malaysia Berhad* and *Takaful Nasional Sdn. Berhad*.

August 1999: RM6,000 million), accounting for 93.4% of gross funds raised during the period. Funds raised through the issuance of *Khazanah* bonds, however, declined to RM680 million (January-August 1999: RM1,393 million). During the same period, redemption of RM2,364 million was recorded, comprising RM2,350 million from MGS and RM14 million from Malaysia Savings Bonds.

The higher net funds of RM15,239 million raised by the private sector was dominated by funds raised through PDS, amounting to RM17,698 million to account for 80.3% of gross funds raised by the private sector. This reflected the increased recourse to PDS as an alternative source of financing. *Cagamas* bonds continued to dominate the PDS market, accounting for RM6,591 million or 37.2% of total PDS. Net redemption during the period amounted to RM6,813 million, comprising redemption of PDS and *Cagamas* bonds at RM4,263 million and RM2,550 million, respectively. Funds raised through equity issues also increased sharply by 189.4% to RM4,353 million (January-August 1999: RM1,504 million), reflecting recourse to the equity market to finance activities as economic conditions improved.

Cagamas

Cagamas Berhad, the national mortgage corporation, raised a total of 39 issues valued at RM18,448 million during the first eight months of 2000 (January-August 1999: RM18,555 million from 28 issues). Funds mobilised during the period comprised RM11,857 million notes from 18 issues and RM6,591 million bonds from 21 issues. Housing loans purchased by *Cagamas* increased sharply by 59% to RM5,476 million during the period (January-August 1999: RM3,445 million), mainly due to the pick-up in the purchase of residential property. The prevailing low interest rates have benefited house buyers as financial institutions competed to offer various attractive housing loan packages. Industrial property loans as well as hire-purchase financing and leasing also picked up in consonance with the economic recovery, increasing to RM224 million and RM2,650 million, respectively (January-August 1999: RM171 million and RM1,676 million, respectively).

Capital Market

Total net funds raised during the first eight months of 2000 were significantly higher (831.7%) at RM23,245 million (January-August 1999: RM2,495 million), with the private sector accounting for RM15,238 million (65.6% of total net funds) and the public sector the balance, as shown in *Table 8.10*. The higher net funds raised by the public sector was mainly due to the 61.5% increase in the issuance of MGS to RM9,691 million (January-

Table 8.10

Funds Raised in the Capital Market (RM million)

	January-August	
	1999 ^P	2000 ^P
By Public Sector		
Debt Securities		
Malaysian Government Securities	6,000.0	9,690.7
Khazanah Bonds	1,392.6	680.3
Government Investment Issues	2,000.0	0.0
Malaysia Savings Bonds	0.0	0.0
New Government debt securities	9,392.6	10,371.0
Less: Redemptions		
Malaysian Government Securities	4,150.0	2,350.0
Government Investment Issues	2,000.0	0.0
Malaysia Saving Bonds	1.7	14.2
Net funds raised	3,240.9	8,006.8
By Private Sector		
Shares ¹		
Public issues	95.5	742.3
Rights issues	1,070.8	2,791.3
Private placements	124.2	691.4
Special issues	200.5	68.5
Warrants	13.5	59.6
New Share Issues	1,504.5	4,353.1
Debt Securities ² (gross)		
Straight bonds	660.0	4,702.0
Convertible bonds	355.8	1,690.1
Islamic bonds	900.0	4,715.0
Bond with warrants	500.0	0.0
Cagamas bonds	4,105.0	6,591.0
New debt securities	6,520.8	17,698.1
Less: redemptions		
Private Debt Securities ³	3,950.9	4,262.6
Cagamas bonds	4,820.0	2,550.0
Net issues of debt securities	-2,250.1	10,885.5
Net funds raised	-745.6	15,238.6
Total net funds raised	2,495.2	23,245.4

^P Preliminary data.

¹ Excludes funds raised by the exercise of Employees Share Option Scheme, Transferable Subscription Rights, Warrants and Irredeemable Convertible Unsecured Loan Stocks.

² Excludes debt securities issued by banking institutions.

³ Includes straight bonds, bond with warrants, convertible bonds and Islamic-based bonds.

Source: Bank Negara Malaysia.

Rating Agencies

The number of ratings completed by **Rating Agency Malaysia (RAM)** surged 71.4% to 48 proposed PDS issues valued at RM18,358 million in the first nine months of 2000 (January-September 1999: 28 PDS issues worth RM28,212 million). The low interest rate regime, the sustained momentum of the economic recovery and the on-going corporate debt restructuring process were factors which contributed to the active primary market. The relatively lower cost of financing also attracted more issuers to tap the bond market. Reflecting the improving corporate credit risk profile, the average spreads for 5-year AA-rated and above PDS *vis-à-vis* MGS of the same tenure tightened from 228 - 299 basis points in 1999 to 160 - 215 basis points in 2000. Similarly, the average spreads for 5-year A-rated PDS declined from 372 basis points to 314 basis points in the same period. A major proportion of the proposed PDS issues was in the A-rated and above categories. The tenure of proposed PDS issues ranged from two to 18 years. Of the PDS ratings completed during the period, 35 were long-term issues while 13 were short-to medium-term issues. A large proportion of the bonds rated was from the infrastructure and utilities sector with 20 proposed PDS issues valued at RM9,677 million.

The **Malaysian Rating Corporation (MARC)** completed a total of 20 ratings of corporate debt valued at RM12,069 million during the first nine months of 2000 (January-September 1999: 15 ratings valued at RM6,187 million). Of these, 11 were Islamic PDS issues valued at RM8,816 million, with two of them being landmark issues in terms of the highest rating assigned and size of Islamic debt issues, rated at RM1,500 million and RM1,100 million, respectively. The PDS rated were from various sectors of the economy, including shipping, construction, property, infrastructure and water utility sectors. In terms of the maturity profile, there were 16 long-term issues and two medium-term issues while another two had combinations of short-and long-term tenure. The preference for medium-to long-term issues arose as market participants sought to lock in the currently attractive cost of funding, particularly for longer term project financing.

Kuala Lumpur Stock Exchange

The performance of the **Kuala Lumpur Stock Exchange (KLSE)** began the year on a positive note. The benchmark Kuala Lumpur Composite Index (KLCI) breached the 950-point level in mid-January. Bullish sentiments continued into February, underpinned by further improvement in economic data and corporate earnings and aided by ample liquidity in the financial system. KLCI breached the 1,000-point level on 17 February to peak at 1,013.27 points on 18 February.

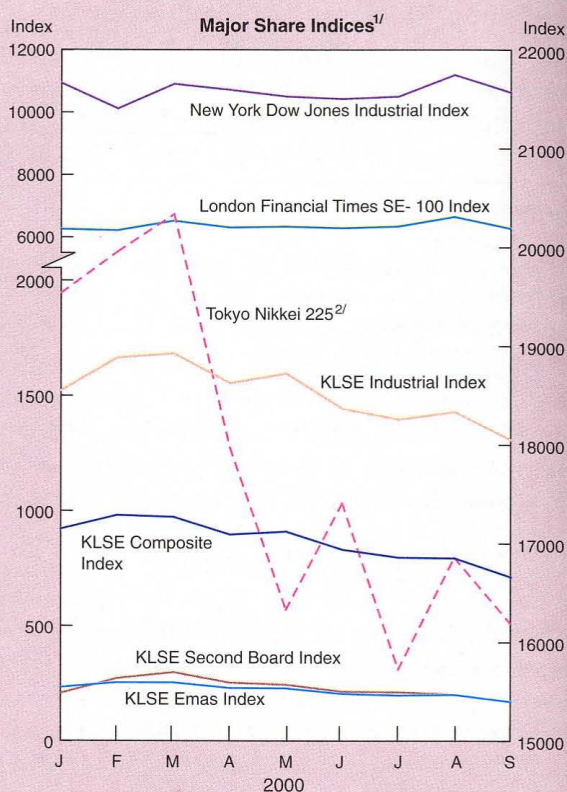
The strong recovery of KLSE at the beginning of the year, however, could not be sustained as KLCI trended downwards in the second and third quarters in line with the performance of other regional bourses. Among the factors contributing to the weak global market sentiments were concerns about US interest rate hikes, the release of lower than expected earnings of some key index-linked stocks and declines in US stock market as well as regional stock markets. KLCI, however, began to pick up in October to close at 766.18 points on 16 October, as shown in *Table 8.11*.

In spite of the downward trend, KLCI continued to outperform most of the regional stock market indices. During the period January to 16 October 2000, KLCI declined by only 8%, compared with Stock Exchange of Thailand Index (-48.2%), the Korean Composite Index (-48%), Jakarta Composite Index (-41.2%), Philippines Composite Index (-40%), Taipei Weighted Index (-36%), Singapore Straits Times Index (-26%) and the Nikkei Index (-18.4%).

During this period, trading volume transacted on KLSE was lower by 17.3%, totalling 62,490 million units (January to mid-October 1999: 75,570 million units) while average daily turnover was 320 million units (January to mid-October 1999: 386 million units). Market capitalisation, however, increased by 6.6% to RM519,465 million at mid-October 2000 (mid-October 1999: RM487,210 million).

In terms of sectoral performance, the trading and services sector accounted for 23.4% of total trading volume, followed by the loans and transferable subscription rights and warrants sector (23.1%)

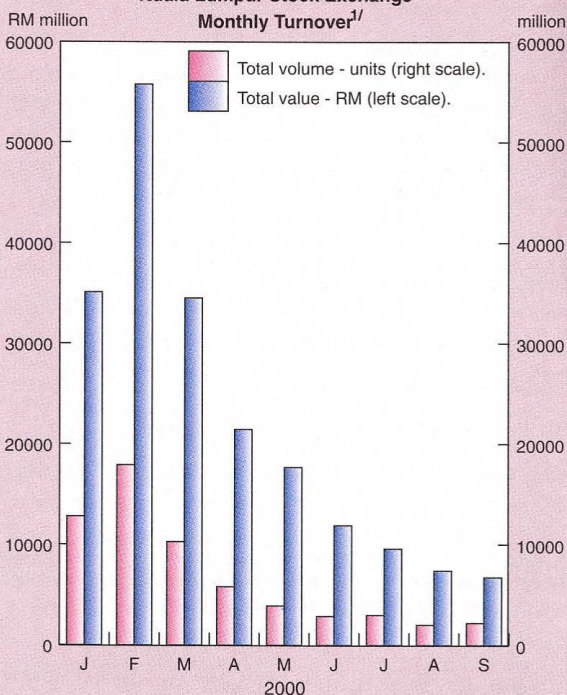
Chart 8.2
Share Markets



1/ End of period closing indices.

2/ Right scale.

**Kuala Lumpur Stock Exchange
Monthly Turnover^{1/}**



1/ Refers to the Main Board and Second Board of the Kuala Lumpur Stock Exchange.

Table 8.11

Kuala Lumpur Stock Exchange: Selected Indicators

	January-Mid October	
	1999	2000
Price indices ¹		
Composite	721.18	766.18
Emas	186.12	185.52
Second board	158.92	177.92
Total turnover ²		
Volume (million units)	75,570	62,490
Value (RM million)	159,860	206,050
Average daily turnover ²		
Volume (million units)	385.57	320.46
Value (RM million)	815.62	1,056.69
Market capitalisation ¹ (RM million)	487,210	519,465
Market capitalisation ¹ /GDP (%)	162.2	159.8
Total no. of companies listed ¹	746	789
Main board	462	490
Second board	284	299
Market liquidity ¹		
Turnover value/Market capitalisation (%)	32.8	39.7
Turnover volume/No. of listed securities (%)	46.0	33.0
Market concentration ¹		
10 most highly capitalised stocks/market capitalisation (%)	33.1	35.6
Average paid-up capital of stockbroking firms ¹ (RM million)	102.19	128.45

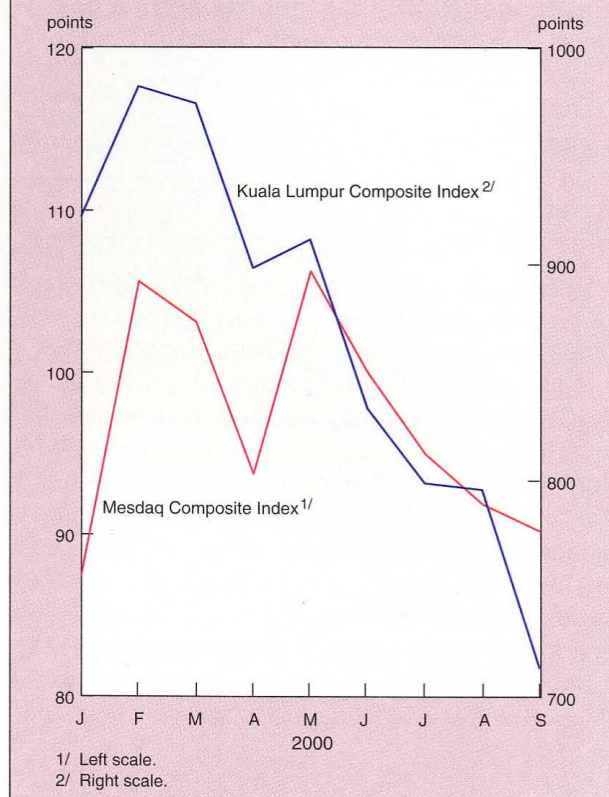
¹ As at end of period.

² Market transactions only.

Source: Kuala Lumpur Stock Exchange.

and industrial products (15.9%). During the first nine months of the year, 31 companies with a combined capital of RM327 million were listed on the KLSE (January-September 1999: nine companies with a combined capital of RM349 million), bringing the total to 788 at end-September 2000 (end-September 1999: 745 companies).

Chart 8.3
Movement of Mesdaq Composite Index (MCI)
against the Kuala Lumpur Composite Index (KLCI)



MESDAQ

The movement of the Malaysian Exchange of Securities Dealing and Automated Quotation (**MESDAQ**) Composite Index (MCI) was broadly in line with the KLCI, beginning the year on improved market sentiments to close at 87.50 points at end-January 2000 (end-December 1999: 85.94 points). MCI has, since June, trended downwards to close at 90.23 points at end-September. Trading volume on MESDAQ amounted to 1.3 million units valued at RM4 million during the first nine months of 2000. MESDAQ continues to undertake measures to promote and market the Exchange. They include introducing a new internet-based trading system, MESDAQ Order Routing and Executive System (MORE) to replace the existing trading system, MESDAQ Quotation System (MQS) and working towards a link-up with KLSE's trading network. MESDAQ is also cooperating closely with various organisations, including the Malaysian Venture Capital Association (MVCA) to promote MESDAQ as an exchange of choice for technology and growth companies in Malaysia.

Table 8.12

Unit Trust Industry: Selected Indicators

	Government Supported Funds	Private Funds	Total	Government Supported Funds	Private Funds	Total
	1999 ¹			2000 (end-July)		
Number of unit trust management companies	10	23	33	10	24	34
Number of unit trust funds ²	29	72	101	30	83	113
Units in circulation (million)	37,104	15,528	52,632	39,901	21,307	61,208
Number of accounts (million)	7.947	0.963	8.910	8.373	1.094	9.467
Net asset value (NAV) (RM million)	31,955	11,058	43,013	35,263	13,738	49,001
NAV/KLSE market value (%)	5.78	2.00	7.78	6.37	2.48	8.85

¹ End of period.² Refers to funds already launched.

Source: Securities Commission.

Unit Trust Industry

The unit trust industry continued to expand in 2000 in consonance with the improving economy and incomes. Twelve new funds were launched in the first eight months of the year (1999: 12 funds), including the RM3,000 million *Amanah Saham Malaysia* fund by *Permodalan Nasional Berhad*, bringing the total number of unit trust funds to 113, as shown in *Table 8.12*. Units in circulation rose 16.3% to 61,208 million units at end-August 2000 (end-1999: 52,632 million units). The increase in the number of funds launched and units in circulation contributed to the 13.9% increase in the net asset value (NAV) of the unit trust industry to total RM49,001 million (end-1999: RM43,013 million). Similarly, the ratio of the unit trust industry's NAV to KLSE market capitalisation was higher at 8.9% (end-1999: 7.8%).

Key Capital Market Measures

The Securities Commission (SC) and KLSE introduced several regulatory and legislative measures during the first nine months of the year aimed at further broadening and deepening the capital market, in addition to promoting its efficiency, transparency, resilience and competitiveness. The key measures were as follows:

Capital Market Master Plan

A comprehensive Capital Market Master Plan is being developed to chart the strategic positioning and future direction of the capital market. Among other things, the master plan aims to address weaknesses that became evident during the financial crisis, provide a strategic road map to

facilitate future business development and assist in the creation of a resilient and competitive capital market.

Consolidation of the Stockbroking Industry

The consolidation exercise is aimed at strengthening the domestic capital market and making it more efficient, cost-effective and resilient to face the challenges of globalisation and liberalisation. In April 2000, SC announced the policy framework for the consolidation of 62 stockbroking companies (SBCs) as a follow up to the earlier initiatives to encourage mergers. SBCs are allowed to find their own merger partners and to determine their own valuation. The objective is to form a core of well-capitalised Universal Brokers which will be allowed to offer a full range of capital market services. In addition to the Budget 2000 tax incentives to encourage the consolidation of the stockbroking industry, Universal Brokers are allowed, effective 1 July 2002 to open branches subject to SC's approval. The tax incentive period has been extended for another year to end-December 2001. SBCs which meet the end-December 2000 deadline can utilise up to 50% of tax losses of the acquired SBC as tax credit to be used within two years as well as stamp duty and real property gains tax exemptions. SBCs which execute firm merger agreements after the 2000 deadline will, however, qualify for a shorter utilisation of the tax credit to within one year.

Corporate Bond Market

Effective 1 July 2000, SC became the single regulatory authority for the supervision and regulation of the corporate bond market. SC introduced several new guidelines and regulations pertaining to PDS. Among others, these guidelines include speedier approval, liberalisation in terms of waiving the mandatory requirement, greater transparency on the circumstances under which the issuance of PDS would be allowed or disallowed, lower cost, removal of restrictions on repo transactions in PDS, greater flexibility on the issuance of PDS as provided under the Shelf Registration Scheme as well as introducing restrictions on the utilisation of PDS proceeds for the development of certain properties.

Equity Market

Effective 1 July 2000, SC became the approving and registering authority for prospectus of all equities and equity-linked issues. SC also allowed companies listed on the KLSE that are undertaking restructuring exercises to issue convertible loan stocks at nominal values of less than RM1. This is to facilitate the raising of capital by listed companies in distress. To ensure that the capital market remains competitive, commission rates were liberalised. In the first stage, effective 1 September 2000, commission rates for all trades above RM100,000 are fully negotiable while trades of RM100,000 and below will be subject to a fixed rate of 0.75%. In the second stage, effective 1 July 2001, commission rates will be fully negotiable for all trades, subject to a cap of 0.7% while other transaction costs will be reduced, including the Securities Clearing Automated Network Services (SCANS) clearing fee, the System Computerised Order Routing and Execution (SCORE) fee as well as the SC levy. New guidelines on advertising were issued on 19 September 2000, whereby, issuers offering securities for sale need not seek prior consent of SC when carrying out certain preparatory work in relation to any proposed offer of securities. KLSE is also finalising a comprehensive review of fees for dealers and remisiers. On 15 May 2000, KLSE launched the technology sector with a corresponding technology index as part of its developmental efforts to assist investors to track technology stock investment. A shorter settlement period from T+5 to T+3 is targeted for implementation in December 2000, which will benefit industry participants and investors and is in line with international best practices.

Fund Management Industry

SC revised the Guidelines on the Establishment of Foreign Fund Management Companies to incorporate two main policy changes, namely the inclusion of investment advisory services and the reduction in the amount of funds sourced from within Malaysia to US\$50 million from US\$100 million before a joint-venture foreign fund management company can apply to manage local unit trust funds.

Framework for the Implementation of Electronic Commerce

SC has commenced work to develop a framework necessary to enable the orderly and effective implementation of electronic commerce (e-commerce) in the capital market. A Working Group on Electronic Commerce in the Capital Market was established on 8 June 2000, comprising representatives from market institutions and industry associations, to study SC's recommendations on e-commerce and to develop the physical and regulatory infrastructure necessary to promote the use of technology in the capital market.

Disclosure-Based Regulation

During the first nine months of 2000, both SC and KLSE issued several guidelines and requirements pertaining to disclosure-based regulation (DBR) aimed at ensuring that investors have timely, adequate and accurate information to make informed investment decisions on companies. KLSE issued Practice Note No. 1/2000 effective 1 April 2000 aimed at strengthening disclosure requirements for internet-related businesses or e-commerce activities of public-listed companies (PLCs). KLSE also established a Taskforce on Internal Controls in May 2000 responsible for the formulation and issuance of guidelines to assist PLCs in reporting the state of internal controls in their annual reports. This is in line with the recommendations of the Finance Committee in its Report on Corporate Governance that PLCs report on the state of their internal controls.

New guidelines were also issued by SC specifying the minimum content requirements for prospectus of unit trusts, debentures and trust deeds. Effective 10 May 2000, SC allowed flexibility to the requirement for chain listing and par value of ordinary shares for primary listing aimed at further facilitating the move towards a disclosure-based regulatory framework.

Corporate Governance and Shareholder Protection

SC introduced a Code of Conduct for Market Institutions on 25 May 2000. The Code laid down the principles of conduct and best governance

practices for market institutions and decision-makers within the institution and its personnel.

Futures Market

The performance of the **Kuala Lumpur Stock Exchange Composite Index Futures (KLSE CI Futures)** on the Kuala Lumpur Options and Financial Futures Exchange (KLOFFE) declined by 22.9% to 286,294 contracts during the first nine months of 2000 (January-September 1999: 371,147 contracts). Lack of foreign participation since September 1998 contributed to the lower trading volume in the KLSE CI Futures. The Derivatives Liquidity Ratio, which measures the volume of futures contracts to the turnover volume of the component stocks, however, improved to 50.8% at end-September 2000 (end-September 1999: 38.5%). In terms of market participation, domestic retailers were the leading players, accounting for 50% of total trade, followed by local members with 27% of total trade, foreign institutions with 17% and other market participants with 6%.

KLOFFE is planning to introduce the Kuala Lumpur Stock Exchange Composite Index Options (KLSE CI Options) contract by year end, making it the first bourse in ASEAN to offer domestic-based index options trading. To further enhance efficiency and competitiveness, KLSE which is the holding company of KLOFFE, has signed a Memorandum of Understanding with the Commodity and Monetary Exchange of Malaysia (COMDEX) in March 2000 regarding the possible merger between the two Exchanges. KLOFFE is also studying the possibility of introducing new products, in particular an index futures based on Islamic principles, aimed at further developing the futures market.

The 3-month **Kuala Lumpur Interbank Offered Rate (KLIBOR) futures** contract was actively traded on COMDEX, increasing by 78% to 35,433 contracts during the first nine months of 2000 (January-September 1999: 19,907 contracts). The higher trading activity during the period can be attributed, in part, to the revival of the market maker scheme since August 1999. Under this scheme, four domestic banks are allowed to quote market prices for the buying and selling of KLIBOR futures contract, thereby facilitating the entry or exit by other market participants.

Stable short-term interest rates that have prevailed since January 2000 led to a decline in the demand for hedging against interest rate movements, particularly in April when average daily turnover declined to 93 contracts as compared to a peak of 226 contracts in January. Interest in KLIBOR futures contracts began to surge in July, following BNM's decision to increase interbank rates by 25 basis points. Increased activity in the local bond market as well as the interest rate swap market contributed to a greater usage of the KLIBOR futures market. Trading volume increased by 140.8% to 7,687 contracts in August (June 2000: 3,192 contracts). In terms of market participation, the most dominant players continued to be banking institutions, both local and foreign banks operating in Malaysia, accounting for 94.3% of total trade during the period.

Trading in **crude palm oil (CPO) futures** declined by 25.9% to 226,910 contracts equivalent to 5.67 million tonnes during the first nine months of 2000 (January-September 1999: 306,121 contracts

equivalent to 7.65 million tonnes). The decline in CPO futures trading can be attributed to the lack of participation from investors as prices of CPO futures had declined to levels where the difference between market prices and future prices was minimal. In addition, the prevalent excess stock has exerted downward pressure on prices. Palm oil prices fell from an average of RM1,460 per million tonne in 1999 to the current level of RM924 as at end-September 2000.

Foreign participation increased slightly to account for 14.8% of total trade during the first nine months of the year (January-September 1999: 12.8%). COMMEX continued to undertake promotional and educational campaigns to attract interest in CPO futures market, including the possibility of relaunching the Crude Palm Kernel Oil (CPKO) futures which was launched in 1992 but subsequently discontinued in 1994 due to the lack of participation. The possibility of launching bond futures based on MGS is also being considered.